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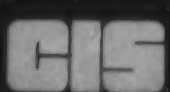

# DESCRIPTION OF POSSIBLE WAYS AND MEANS COMMITTEE AMENDMENTS

# TO H.R. 4170 (TAX REFORM ACT OF 1983)

Scheduled for Committee Markup

on February 29, 1984

Prepared by the Staff of the Joint Committee on Taxation

February 29, 1984

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## INTRODUCTION

This document provides a brief description of possible further Ways and Means Committee amendments to H.R. 4170 (Tax Reform Act of 1983), as reported by the Committee on October 21, 1983 (H. Rep. No. 98-432).

The possible additional amendments to H.R. 4170 described in this document are: (I) miscellaneous changes to existing titles of H.R. 4170; (II) effective date changes to H.R. 4170 provisions; (III) additional revenue-raising items; and (IV) highway use tax alternatives. The revenue raising items include: (A) a "tax freeze" proposal; (B) partnerships and other pass-through entities; (C) taxation of corporations and their shareholders; (D) time value of money and other accounting issues; (E) debt obligations; (F) compliance provisions; (G) employer/employee benefit provisions; (H) miscellaneous provisions relating to tax-motivated transactions; and (I) tax straddles.

This document does not include a description of previously approved Committee amendments to H.R. 4170 (technical corrections and miscellaneous provisions approved on November 16, 1983).

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| Item | Committee Bill | Suggested Change |
|---|---|---|
| Title I--Tax-Exempt Entity Leasing | The bill contains rules relating to allocations by partnerships with both taxable and tax-exempt partners. | The language of that provision would be clarified. |
| Title II--Life Insurance Tax Act of 1984 | | |
| 1. Dividends received deduction (sec. 805(a)(4)) | The bill allows a company the full dividends-received deduction for 100-percent dividends, except to the extent that such dividends are distributions out of tax-exempt interest or dividends which are not 100-percent dividends. | Extend similar treatment to dividends received by a foreign company which would be 100--percent dividends if section 1504(b)(3) did not apply for purposes of section 243(b)(5). |
| 2. Definition of "tentative LICTI" for a controlled group (sec. 806(c)) | The bill provides that all life companies in a controlled group shall be treated as one life company for purposes of computing the tentative LICTI for the group, whether or not the group can file a consolidated return. | Provide specific regulatory authority for the Secretary to prescribe proper adjustments to be made in the application of this provision so that a loss from operations of any member of a group will reduce the tentative LICTI from such group only once. |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| 3. Computation of tax reserves and prescribed method (sec. 807(d)(3)(iii). | The bill provides that the tax reserve method for noncancellable A&H contracts is a 2-year full preliminary term method. | Provide a special rule to allow a company to use the net level reserve method in computing reserves for noncancellable A&H, for tax purposes, if it was using such method as of 12-31-82 and continues to use such method for annual statement reporting purposes. |
| 4. Computation of tax reserves and use of prevailing commissioners' standard tables (sec. 807(d)(5)). | The bill provides a special rule for contracts issued before 1948 when no commissioners' standard tables were issued. | In addition to the current special rule for contracts issued before 1948, (1) provide general regulatory authority to prescribe appropriate tables if no standard table is applicable when a contract is issued, and (2) require the use of the table which generally yields the lowest reserves if there are multiple prevailing commissioners' standard tables that can be used for a particular reserve. |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| 5. Computation of an additional reserve for qualified substandard risks (sec. 807(e)(5). | The bill provides that a qualified substandard risk means any substandard risk if, among other things, "the net surrender value under the contract may not be used to systematically pay premium charges for such risk." | Clarify that a substandard risk meets this requirement if "the net surrender value under the contract is not regularly used to pay premium charges for such risk." |
| 6. Determination of the equity base for purposes of applying the differential earnings rate (sec. 809(a)(4)). | The bill provides that a company's equity base shall include the excess of statutory reserves over tax reserves. | Clarify that for purposes of computing the equity base, statutory reserves shall not include any reserve attributable to deferred and uncollected premiums if such items have not been included in life insurance gross income. |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| 7. Definition of company's share and policyholders' share (sec. 812(f)). | The bill provides that the term "gross investment income" shall not include 100-percent dividends. | Clarify that the term also shall not include any dividends that would be 100-percent dividends but for the fact that the recipient is a foreign company. |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| 8. (a) Reserves computed on the new basis: fresh start (bill sec. 216(b)(2)). | The bill provides that no adjustments attributable to a change of basis in computing reserves before 1984 shall be taken into account after 1983. | Retain the same provision with respect to decreases in reserves. Modify the provision with respect to increases in reserves to to allow such adjustments to be taken into account to the extent that the amount of the adjustments that would be taken into account after 1983 exceeds the amount of any fresh start adjustment allowed under the bill with respect to the contracts to which reserve increase was attributable. Also, clarify that no premium income shall be recognized to the extent such premium is directly related to an increase in reserve adjustment disallowed under the provision as modified. |
| (b) Reinsurance transactions, etc., after September 27, 1983 (bill sec. 216(b)(3)). | The bill provides that the fresh start provisions would not apply to reserves transferred (or expenses transferred) under reinsurance agreements entered into, modified, or terminated, nor to reserve strengthening, after September 27, 1983. | Clarify that denial of the fresh start relates only to such activities occurring after September 27, 1983, and before January 1, 1984. |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| 9. Transitional rules for life insurance contracts issued during 1984 (sec. 7702(i)(1)). | The bill provides that any contract issued during 1984 shall be treated as meeting the requirements of the new definition of life insurance if such contract would meet the present requirements of section 101(f) or if such contract (that is not a flexible premium contract) would meet the requirements of the new cash value accumulation test by substituting 3 percent for 4 percent. | Expand the transitional rules to cover any contract issued during 1984 pursuant to an existing plan of insurance if the contract (whether or not a flexible premium contract) would meet the requirements of section 101(f), or if such contract would meet certain definitional rules provided for irreplaceable life contracts. |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| 10. Limitation on interest deduction in case of life insurance loans (sec. 264(d)). | The bill provides an overall limitation on interest deduction in the case of life insurance loans determined by multiplying the annual deficiency interest rate by the applicable dollar amount. For individuals, the applicable dollar amount would be $250,000 ($500,000 for a joint return); for corporations, etc., the applicable dollar amount would be $500,000 x the number of qualified lives. | Clarify that a qualified life means any individual for which the corporation, etc., held a policy of life insurance, had an outstanding life insurance loan, and the face amount of such policy is not less than 10 percent of the highest face amount of a policy carried by the corporation, etc., on the life of an individual having an outstanding life insurance loan. |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| **Title IV--Simplification** | | |
| 1(a). Transfer of property between spouses or incident to divorce (sec. 422) | Transfers of property between spouses or incident to divorce will be non-taxable, carryover basis transactions. | Clarify that investment tax credit will not be recaptured. |
| (b). Gift and estate tax treatment (sec. 426) | Under present law, there is no gift tax liability for transfers of property to spouse in settlement of marital or property rights pursuant to written agreement where divorce occurs within 2 years of agreement.<br><br>The bill provides estate tax deduction for transfers pursuant to these written agreements. | Extend rules to cover transfers pursuant to agreements executed within one year after divorce occurs. |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| 2. "At-risk" rules for losses. (sec. 432) | The bill provides that an active trade or business of a subchapter C corporation (other than a personal holding company or personal service corporation) will not be subject to any at-risk rules. A trade or business will be required to have three, full-time non-owner employees, one full-time employee actively managing the business, and its "out-of-pocket" business expenses must exceed 15 percent of gross income. | (1) The corporate partner rules would be expanded to apply to all general corporate partners.<br><br>(2) The present rules relating to the treatment of personal holding companies as not being a component member of an affiliated group of corporations would be eliminated and replaced with a rule that the income of a personal holding company could not be offset by the losses allowed by reason of the trade or business exception to the at-risk rule. |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| 3 (a). Definition of resident alien. (sec. 451) | Green card holders may be present in the United States for up to ten days without losing nonresident alien (NRA) status. | The ten-day exception would not apply to green card holders. |
| | The bill treats certain students, teachers, and diplomats (including employees of international organizations) as NRAs unless they intend permanently to reside here. | Delete the intent exception. All these individuals would be NRAs. |
| | The bill treats certain individuals as NRAs if they are teachers, students, or diplomats at all times when present here. An individual present for 183 days on a diplomatic visa and one day on a tourist visa would be a resident for the year. | Days present as a teacher, student, or diplomat would not count as days of presence (against the 183-day test). |
| 4. Treatment of certain related party transactions (sec. 492) | Applies the present law rules denying losses between related parties to transactions between controlled corporations (using a 50-percent control test). | Would not apply to transactions with a controlled DISC. |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| **Title VI--Technical Corrections** | | |
| 1. Alternative minimum tax (sec. 611(a)) | TEFRA provided that income from limited partnership interests, etc. is investment income for purposes of computing the amount of "below the line" interest allowed in computing the minimum tax. | Clarify that this rule applies whether or not the deductions from the limited partnership interest exceeds the income. |
| 2. TRAC leases (sec. 612(d)) | The bill made the TRAC provision of TEFRA inapplicable where the lessee treated itself as the owner for tax purposes. | The provision in the bill would apply only where the lessee treated itself as the owner (for some or all tax purposes) and the lessor did not treat itself as the owner. |
| 3. Section 304--Related corporation transactions (sec. 612(k)) | The bill provides that the assumption of liabilities by a corporation of acquisition debt to a related party may give rise to dividend treatment. | It would be clarified that this rule would not apply where the creditor had terminated its interest in the corporation (under rules similar to the rules relating to redemptions); the provision in the bill would not apply to transactions before October 21, 1983. |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| 4. Targeted jobs credit | Present law is unclear as to whether a qualified summer youth or a cooperative education youth who continues to work for the same employer, after the summer, as a member of another targeted group is required to submit to a second determination of whether the youth is economically disadvantaged. | The original determination that a qualified summer youth or cooperative education youth is economically disadvantaged would continue to be valid with respect to the eligibility of the individual as a member of another targeted group, if the individual continues to work for the same employer. |
| 5. Subchapter S | | |
| (a). Post-termination period deduction (Code sec. 1371(e)) | Present law allows tax-free cash distributions during a "post-termination" period. | Allow corporations to elect to make taxable distributions during this period. |
| (b). Application of corporate preference rules to S corporations (Code sec. 291) | Section 291 is inapplicable to S corporations. | Apply section 291 to S corporations during the first 3 years after change of status from C corporation status. |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| (c). Accounting for year election terminates. (Code sec. 1362(e)(2) | Present law provides a pro-rata allocation of income for the full year in which an election terminates unless shareholders consent to closing the books. | Make the pro-rata allocation inapplicable where more than 50 percent of stock is sold or exchanged during termination year. |
| (d). Accumulated adjustments amount (Code sec. 1368) | Present law provides for tax-free distributions to extent of amount in an "accumulated adjustments account," which is essentially an amount equal to undistributed income. | Clarify that the account could be negative; all distributions during the year would reduce the account proportionately; and the account could be reduced by non-deductible expenses other than those related to producing tax-exempt income |
| 6. Certain Leased Employees | If a business uses "leased" employees, then the leased employees are generally treated as employees of the business in testing whether a pension plan of the business meets the nondiscrimination standards for tax qualification. A safe harbor exception is provided if the leasing company has a pension plan that meets special standards. Recently, some businesses have taken the position that the exception applies to their own, common-law employees if those employees are nominally employed by a leasing company. | The safe harbor for leased employees could be clarified to indicate that a common-law employee of a business must be taken into account as an employee of the business without regard to the safe harbor rule. |

SOCIAL SECURITY TECHNICAL AMENDMENTS TO H.R. 4170

| Item | House Bill | Suggested Change |
|---|---|---|
| Title VI--Technical Corrections | | |
| Coverage of Federal Employees with Breaks in Service (bill secs. 641 and 643) | Requires social security coverage for employees entering or re-entering civilian Federal service after military service | Limit amendment so that civilian employees not previously under social security can serve in the military and return to civil service without changing their status as CSRS participants; |
| | Current law also requires social security coverage after a year break in service for Federal employees even if that employment was a tour of duty on behalf of the Federal government(i.e. in international organizations) | Allow service for international organizations to count as non-covered service, to prevent unintended disruption in Federal pension system status |

SOCIAL SECURITY TECHNICAL AMENDMENTS TO H.R. 4170

| Item | Present Law | Suggested Change |
|---|---|---|
| Title VI--Technical Corrections | | |
| Coverage of legislative branch employees (bill sec. 641(j)) | Allows Congressional staff to be exempt from either CSRS or OASDI coverage if withdraw from CSRS after Dec. 31, 1983 | Requires coverage under one plan or the other if re-enter legislative branch employment within 365 days; OASDI coverage is required if break is longer than 365 days |
| | Exempts from OASDI coverage only those legislative branch employees actually covered by CSRS on Dec. 31, 1983, whether in Congressional or executive branch employment, or as CSRS annuitants | Conforms treatment of those covered by non-CSRS Federal retirement systems (e.g. State Dept., CIA) to that of employees and annuitants covered by CSRS |

SOCIAL SECURITY TECHNICAL AMENDMENTS TO H.R. 4170

| Item | Present Law | Suggested Change |
|---|---|---|
| Title VI--Technical Corrections | | |
| c. Congressional Panel on Social Security Organization (bill sec. 642) | Reimbursement for panel members for travel and compensation per day is not allowed under current law, contrary to specific language in P.L. 98-21 | Allows travel expenses to be paid according to Senate procedures; allows panel members to be paid if they are re-employed annuitants |

| Item | Committee Bill | Suggested Change | |
|---|---|---|---|
| Title VII--Tax-Exempt Bonds | | | |
| 1. Exception from volume cap for certain bonds | The Committee bill imposes a $150 per capita volume cap on the IDBs and student loan bonds that a State can issue during any year. A Committee amendment to the bill provides an exception to the volume cap in the case of bonds to finance multi-family housing. | The proposal is to provide another exception to the volume cap for bonds which meet the following requirements:<br><br>(1) the bond proceeds are used to finance convention or trade show facilities, airports, docks, wharves, or mass commuting facilities; and<br><br>(2) the facilities are owned by a governmental unit (i.e., no cost recovery deductions or tax credits are allowable with respect to the facilities). | |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| 2. Repeal of advance refunding of certain IDBs | IDBs for convention or trade show facilities, airports, docks, wharves, mass commuting facilities, or parking facilities may be advance refunded. | Prohibit advance refunding of such facilities.<br><br>Effective date.--Refunding bonds issued after the date of enactment. |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| 3. Exception for multi-family housing from volume cap | The Committee amendment provided that IDBs issued to finance multi-family housing projects which meet the Internal Revenue Code rules are exempt from the volume cap. Other provisions of the Committee amendment require multi-family housing projects financed under section 11(b) of the Housing Act to comply with the Code rules. | The proposed amendment would clarify that the volume cap would not apply to any public housing program obligation under section 11(b) of the Housing Act. |
| 4. Preference in volume cap for projects in process | The Committee amendment provides priority in the use of the $150 volume cap for projects which received an inducement resolution prior to October 19, 1983. | The proposed amendment would limit the priority rule to projects which received an inducement resolution after December 31, 1982, and before October 19, 1983. |
| 5. Exception for multi-family housing to Federal guarantee rule | The Committee amendment provided that IDBs issued to finance multi-family housing which meet the rules of the Internal Revenue Code would not be subject to the restriction on combining tax-exempt financing with Federal guarantees. Other provisions of the Committee amendment require multi-family housing projects financed under section 11(b) of the Housing Act to be comply with the Code rules. | The proposed amendment would clarify that the Federal guarantee rule would not apply to a public housing program obligation under section 11(b) of the Housing Act. |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| 6. Exception for certain organizations from Federal guarantee rule | The Committee amendment provides exceptions from the rule prohibiting the combination of tax-exempt financing and Federal guarantee to guarantees by the Federal Housing Administration, the Veterans' Administration, and any guarantee of student loans. | The proposed amendment would provide additional exceptions to the Federal guarantee rule in the case of the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, the Government National Mortgage Association, and the Student Loan Market Assocation. |
| 7. Exception to use of IDBs to finance existing facilities where rehabilitation occurs | The Committee amendment provides an exception to the rule which prohibits IDBs to be used to finance existing facilities in connection with the acquistion of a building where there are rehabilitation expenses of at least 15% of the combined cost of the building and rehabilitation. | The proposed amendment would clarify that the rehabilitation expenses need not be financed from the proceeds of the tax-exempt bond, that the rehabilitation expenses must be incurred by the person acquiring the building, and that the rehabilitation expenses must occur within 2 years of the later of the date of acquisition or the date the obligations are issued. |
| 8. Exception for Multi-family housing to arbitrage rules | The Committee amendment provided that IDBs issued to finance multi-family housing projects which meet the Internal Revenue Code rules are exempt from the arbitrage rules applicable to single-family housing bonds. Other provisions of the Committee amendment require multi-family housing projects financed under section 11(b) of the Housing Act to comply with the Code rules. | The proposed amendment would clarify that the arbitrage rules would not apply to a public housing program obligation under section 11(b) of the Housing Act. |

| Item | Committee Bill | Suggested Change |
| --- | --- | --- |
| **Title VIII-Miscellaneous** | | — |
| 1. Death of military and civilian employees. | A committee amendment provided relief for military and civilian employees dying as the result of injuries sustained overseas. | This provision would be deleted because it passed the House as separate legislaton (H.R. 4206). |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| 2. Capital gains treatment for portion of gain on condominium conversions. | Capital gain treatment is available for appreciation in value of qualifying condominium units prior to determination date, reduced by depreciation recapture. | No change. |
| | Determination date is earliest of<br><br>(1) day on which taxpayer adopted a conversion plan,<br><br>(2) day on which substantial improvments were first made in anticipation of conversion, or<br><br>(3) day on which form of ownership changed to condominium units. | Alternative 1: Determination date would be day on which taxpayer adopted a conversion plan only if such date was not more than 2 years earlier than (2) or (3) at left.<br><br>Alternative 2: Determination date would be day on which taxpayer adopted a conversion plan and converted 10 percent of units, otherwise (if earlier) (2) or (3) at left. |

TECHNICAL CHANGES
TITLE X - Medicare Budget Reconciliation Amendments

| Item | House Bill | Suggested Change |
|---|---|---|
| TITLE X--Medicare Budget Reconciliation Amendments | | |
| 1. Title (bill sec. 1000) | "Medicare Budget Reconciliation Amendments of 1983." | "Medicare Budget Reconciliation Amendments of 1984." |
| 2. Use of accrediting organizations for certain entities furnishing services (bill sec. 1030) | Omitted 1861(f) (psychiatric) hospitals | Add 1861(f) |
| 3. Miscellaneous printing and format errors | | |

## II. EFFECTIVE DATES -- H.R. 4170

| Item | Committee Bill | Suggested Change |
|---|---|---|
| **Title I--Tax-Exempt Entity Leasing** | | |
| 1. Allocations by partnerships, etc. with taxable and tax-exempt entities as partners, etc. | May 23, 1983 | October 21, 1983. (This provision was not contained in H.R. 3110, as introduced on May 23, 1983.) |
| **Title II--Life Insurance Tax Act of 1984** | | |
| 1. Definition of life insurance contract (sec. 7702). | Contracts issued after December 31, 1983. | Clarify that in the case of a master contract, the date taken into account as the issue date with respect to any insured shall be the first date on which such insured is covered under such contract. |
| 2. Group-term life insurance--extension of nondiscrimination rules and $50,000 cap to retired employees (sec. 79). | Apply to taxable years beginning after December 31, 1983, but not to any group-term life insurance plan in existence on September 27, 1983, but only with respect to an individual covered by the plan on such date, and in an amount in excess of the insurance overage of such individual on such date. | Clarify that the provisions also shall not apply to any group-term life insurance plan of the employer (or a successor employer) which is a comparable successor to an existing plan. |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| **Title III--Private Foundations** | | |
| 1. Deduction limitations for contributions to private foundations (bill sec. 302) | Contributions made in taxable years beginning after 1983 (rule on qualified appreciated stock sunsets 12/31/93) | Contributions made in taxable years beginning after 1984 (rule on qualified appreciated stock sunsets 12/31/94) |
| 2(a) Exemption of certain operating foundations from section 4940 excise tax (bill sec. 303(a)) | Taxable years beginning after 1983 | Taxable years beginning after 1984 |
| (b) Exemption of certain operating foundations from section 4945 expenditure responsibility rules (bill sec. 303(b)) | Grants made after 1983 | Grants made after 1984 |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| 3. Reduction in section 4940 excise tax on investment income where payout increases (bill sec. 304) | Taxable years beginning after 1983 | Taxable years beginning after 1984 |
| 4. Amendments to section 4942 payout requirements (bill sec. 305) | Taxable years beginning after 1983 (transitional rule for pre-1984 years) | Taxable years beginning after 1984 (transitional rule for pre-1985 years) |
| 5. Abatement of first tier excise taxes (bill sec. 306) | Taxable events occurring after 1983 | Taxable events occurring after 1984 |
| 6. Definition of family member under section 4946 (bill sec. 307(b)) | January 1, 1984 | January 1, 1985 |
| 7. Annual notice disclosure requirement under section 6104 (bill sec. 307(c)) | January 1, 1984 | January 1, 1985 |

| Item | Committee Bill | Suggested Change |
|---|---|---|
| 8. Amendments to section 4943 excess business holdings divestiture rules (bill secs. 308-311, 315(b)) | Generally, effective dates relate to date of enactment | Same as bill except to extend applicability of provision as to disposition of post-1969 gifts or bequests to cover situations where initial five-year divestiture period ends on or after 11/1/83 |
| 9. Termination of status as substantial contributor (bill sec. 314) | Taxable years beginning after 1983 | Taxable years beginning after 1984 |

| Item | Committee Bill | Proposal |
|---|---|---|
| 1. Individual estimated tax (sec. 411) | Taxable years beginning after December 31, 1983 | Taxable years beginning after December 31, 1984<br><br>Revenue effect.--Comparison with H.R. 4170<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>-.7 +.7 -- -- +.1 |
| 2(a). Treatment of property between spouses or incident to divorce. (sec. 422) | Applies to transfers after date of enactment | Also allow taxpayers to elect to have this provision apply to transfers after December 31, 1983 and on or before date of enactment |
| (b). Alimony. (sec. 423) | Applies to decrees and agreements executed after 1983 | Apply to decrees and agreements executed after 1984<br><br>Revenue effect.<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>* * * * * |

| Item | Committee Bill | Proposal |
|---|---|---|
| (c). Dependency exemption. (secs. 424 and 427) | Applies to taxable years beginning after December 31, 1983 | Apply to taxable years beginning after December 31, 1984 |
| 3(a). Definition of resident alien (sec. 451) | Taxable years beginning after December 31, 1983, with no counting of days of presence before that time unless the alien was a resident under existing law before that time | Apply to taxable years beginning after December 31, 1984, with no counting of days of presence before that time unless the alien was a resident under existing law before that time |
| | Individuals who hold green cards on January 1, 1985 will not be taxable as residents until they re-enter the United States. | Existing green card holders would be taxable as residents starting January 1, 1985, whether or not they re-enter the United States. |
| (b). Treatment of community property income of nonresident aliens. (sec. 452). | Taxable years beginning after December 31, 1983 | Apply to taxable years beginning after December 31, 1984 |

| Item | Committee Bill | Proposal |
|---|---|---|
| 4. Elimination of Government-supplied strip stamps for distilled spirits containers (sec. 473) | Stamps may be used only until January 1, 1985 | Stamps could be used until July 1, 1985 |
| 5. Rollover of certain partial distributions from qualified plans. (sec. 491) | Distributions made after December 31, 1983 | Apply to distributions made after date of enactment |
| 6. Treat certain retailers of gasoline as producers | Purchases after date of enactment. | Purchases after June 30, 1984. |
| 7. Move tax on aviation gasoline to retail level. | Purchases after December 31, 1983 | Purchases after June 30, 1984 |

| Item | Committee Bill | Suggested Change |
| --- | --- | --- |
| Title VI--Technical Corrections | | |
| Section 338 stock purchases (sec. 612(j)) | The provisions are retroactive as if enacted in TEFRA. | The provision relating to the liquidation of an acquired corporation (sec. 269) would apply only to liquidations after October 21, 1983; the change in the definition of purchase and the treatment of consolidated groups would not apply to purchases before October 21, 1983 if the taxpayer elects; and the time for making a section 338 election for purchases before Sept. 1, 1983, would be extended to 60 days after date of enactment |

EFFECTIVE DATES -- H.R. 4170

| Item | House Bill | Suggested Change |
|---|---|---|
| Title VI--Technical Corrections | | |
| Application of Foreign Work Test (bill sec. 641(g)) | Auxiliary benefits will be withheld on the same basis as primary benefits; effective for months after April 1983 | Effective 2nd month after month of enactment of H.R. 4170 |

EFFECTIVE DATES -- H.R. 4170

| Item | House Bill | Suggested Change |
|---|---|---|
| Title VI--Technical Corrections | | |
| . FICA treatment of "Pickup" Plan (bill sec. 644) | The FICA treatment of employee contributions to a state "pickup" plan is effective upon enactment of this Act | Effective as if this provision had been enacted as part of the Social Security Amendments of 1983 |

EFFECTIVE DATE CHANGES
TITLE VI - Technical Amendments Act

| Item | House Bill | Suggested Change |
|---|---|---|
| Title VI--Technical Corrections Subtitle D Part II - Changes in medicare-related provisions of the Social Security Act | | |
| 1. Professional Review Organizations (bill sec. 646) | Requirement that medicare hospitals have an agreement with a transition PSRO by January 1, 1984 | Requires agreement within 60 days after date of enactment of this Act. |
| 2. Group Appeals Under the Provider Reimbursement Review Board (bill sec. 646) | Effective with respect to any appeal brought on or after date of enactment of the Social Security Amendments of 1983 | Any appeal brought on or after date of enactment of the Tax Reform Act of 1984 |
| 3. Medicare prospective payment state waiver regulations (bill sec. 646) | Applied implementation schedule of proposed regulations (Sept.1, 1983) and final regulations (Dec. 31, 1983) to all provisions of medicare prospective payment, including state waivers | Publication of proposed state waiver regulations by May 1, 1984 and final regulations by August 1, 1984 |
| 4. Working Aged Premium Penalty (bill sec. 647) | Effective date for special premium provisions for the working aged 90 days after date of enactment | Effective beginning July 1984 |
| Title VIII-Miscellaneous | | |
| Pre-ERISA cash and deferred plans (sec. 807) | Plan years beginning after December 31, 1983. | Plan years beginning after date of enactment. |

EFFECTIVE DATES -- H.R. 4170

| Item | House Bill | Suggested Change |
|---|---|---|
| Title IX--Social Security Disability Benefit Reform | Bill applies to cases pending in SSA or in court on date of enactment or initiated on or after enactment | Insert "only" into effective date, to insure prospective application of amendment |

EFFECTIVE DATE CHANGES
TITLE X - Medicare Budget Reconciliation Amendments

| Item | House Bill | Suggested Change |
|---|---|---|
| TITLE X--Medicare Budget Reconciliation Amendments | | |
| 1. Payment for outpatient diagnostic laboratory tests (bill sec. 1001) | Establish payment rates based on 60% of prevailing charges for year beginning July 1, 1983 | July 1, 1984 |
| | Statewide/regional option during three year period beginning March 1, 1984 | July 1, 1984 |
| | Effective for services furnished on or after March 1, 1984 | July 1, 1984 |
| 2. Coverage of administration of hepatitis B vaccine (bill sec. 1003) | Effective for services furnished on or after January 1, 1984 | July 1, 1984 |
| 3. Pacemaker reimbursement review and reform (bill sec. 1004) | Regulations effective February 1, 1984 | October 1, 1984 |
| | Secretarial review of reimbursement for physicians' services related to implantation of pacemakers by April 1, 1984 | October 1, 1984 |
| 4. Payment for physicians' services furnished to hospital inpatients (bill sec. 1007) | Roll back physician fees to June 1983 level, effective January 1, 1984. Provide no catch-up when updating July 1, 1984 - June 30, 1985. | Freeze physician fees at June 1984 level, effective July 1, 1984. Provide no catch-up when updating July 1, 1985 - June 30, 1986. |
| | Physician agreements with hospitals effective January 1, 1984 | July 1, 1984 |

| Item | House Bill | Suggested Change |
|---|---|---|
| 5. Removing costs of nurse anesthetists from DRG-based payments (bill sec. 1038) | Effective for cost reporting periods on or after October 1, 1983 and before October 1, 1986 | October 1, 1984 and before October 1, 1986 |
| 6. Determination of hospital area wage index (bill sec. 1039) | Secretary's report due May 1, 1984 | June 1, 1984 |

## III. Additional Revenue Raising Items

### A. TAX FREEZE

| Item | Public Law | Tax Freeze as Originally Proposed | Possible Modifications |
|---|---|---|---|
| 1. Foreign earned income. | The maximum amount of income earned abroad excluded from taxable income is scheduled to increase from $80,000 in 1983, in $5,000 annual increments, to a permanent level of $95,000 in 1986. | The proposal would freeze it at $80,000 until 1987 and increase it, in $5,000 increments, to $95,000 in 1989. | The modification would freeze it at $80,000 until 1988, instead of 1987 and increase it in $5,000 increments, to $95,000 in 1990.<br>Revenue effect.<br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br>1984 1985 1986 1987 84-87<br>* * .1 .1 .2 |
| 2. Expensing. | The amount of personal property which businesses may elect to expense each year is scheduled to increase from $5,000 in 1983 to $7,500 in 1984 and 1985 and to $10,000 thereafter. | The proposal would freeze it at $5,000 through 1986, increasing to $7,500 in 1987 and 1988 and $10,000 thereafter. | The modification would freeze it at $5,000 through 1987, increasing to $7,500 in 1988 and 1989 and $10,000 thereafter.<br>Revenue effect.--<br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br>1984 1985 1986 1987 84-87<br>.2 .4 .4 .4 1.4 |
| 3. Investment credit for used property. | The maximum amount of used property eligible for the investment credit is scheduled to increase from $125,000 to $150,000 in 1985. | The credit would be frozen at $125,000 until 1987. | The credit would be frozen at $125,000 until 1988.<br>Revenue effect.--<br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br>1984 1985 1986 1987 84-87<br>-- * .1 .1 .3 |

| Item | Public Law | Proposal | Possible Modifications |
|---|---|---|---|
| 4. Net interest exclusion. | Starting in 1985, individuals will be able to exclude 15 percent of interest income to the extent such income exceeds certain interest deductions, up to a maximum exclusion of $450 for single persons and $900 for married couples. | The exclusion would be postponed until 1987. | The modification would postpone the exclusion until 1988.<br><br>Revenue effect.--<br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>-- 1.0 2.9 3.1 7.0 |
| 5. Limits on pension plans. | The dollar limits on the contributions to and benefits from tax-qualified pension plans are scheduled to be indexed for inflation in 1986. | The proposal would freeze the dollar limits at current levels until 1987 when they would be indexed. | The modification would freeze the dollar limits at current levels until 1988 when they would be indexed.<br><br>Revenue effect.--<br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>-- -- * 1 .1 |
| 6. Employee stock ownership plans. | The tax credit for employer contributions to an employee stock ownership plan (ESOP) is scheduled to increase from one-half of one percent of payroll in 1983 and 1984 to three-fourths of one percent in 1985. | The proposal would freeze the credit at the present rate through 1986. | The modification would freeze the excise tax at 16 cents until January 1, 1988.<br><br>Revenue effect.--<br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>-- .3 .6 .7 1.7 |

| Item | Public Law | Proposal | Possible modifications |
|---|---|---|---|
| 7. Top estate and gift tax rate. | The maximum estate and gift tax rate is scheduled to be reduced from 60 percent in 1983 to 55 percent in 1984 and 50 percent in subsequent years. | The proposal would freeze the 60-percent rate until 1986 and would reduce the rate to 55 percent in 1987 and 50 percent thereafter. | The modification would freeze the 60 percent rate until 1987 and would reduce the rate to 55 percent in 1988 and 50 percent thereafter.<br>Revenue effect.--<br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br>1984 \| 1985 \| 1986 \| 1987 \| 84-87<br>* \| .1 \| .4 \| .5 \| 1.0 |
| 8. Windfall profit tax on newly discovered oil. | The windfall profit tax rate on newly discovered oil is scheduled to decline from 25 percent in 1983 to 22.5 percent in 1984, 20 percent in 1985, and 15 percent in subsequent years. | The proposal would freeze the 25-percent rate through 1986 and then reduce the rates to 22.5 percent for 1987, 20 percent for 1988 and 15 percent for 1989 and future years. | The modification would freeze the 25 percent rate through 1987 and then reduce the rates to 22.5 percent for 1988, 20 percent for 1989 and 15 percent for 1990 and future years.<br>Revenue effect.--<br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br>1984 \| 1985 \| 1986 \| 1987 \| 84-87<br>* \| * \| * \| * \| * |
| 9. Cigarette excise tax. | The excise tax rate on cigarettes are scheduled to be cut in half (e.g., from 16 cents per pack to 8 cents per pack) after September 30, 1985. | The excise tax rate would be frozen at 16 cents per pack until January 1, 1987. | The modification would freeze the excise tax at 16 percent until January 1, 1988.<br>Revenue effect.--<br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br>1984 \| 1985 \| 1986 \| 1987 \| 84-87<br>-- \| -- \| 1.9 \| 1.9 \| 3.8 |

| Item | Public Law | Proposal | Possible modifications |
|---|---|---|---|
| 10. Telephone excise tax. | The 3-percent telephone excise tax is scheduled to expire after 1985. | The expiration would be delayed until 1987. | The expiration would be delayed until 1988.<br>Revenue effect.<br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br>1984 1985 1986 1987 84-87<br>-- -- 1.2 2.0 3.2 |
| 11. Finance leasing. | Liberalized leasing rules regarding limited use property and fixed price purchase options are scheduled to take effect in 1984. | The proposal would restore pre-1981 law until 1986 effective on January 1, 1984. Transition rules would be provided for cases when construction has already begun or binding contracts have been signed. | The freeze would be modified to restore pre-1981 law until 1988, effective on date of Committee action.<br>Revenue effect.<br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br>1984 1985 1986 1987 84-87<br>.1 .4 1.0 1.5 3.0 |

## B. PARTNERSHIPS AND OTHER PASS-THROUGH ENTITIES

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| 1. Use of allocations to affect income or loss | | | |
| a. Allocations with respect to contributed property | Partners who contribute property to a parnership may elect to allocate income, gain or loss, and depreciation or depletion to reflect variations between the basis of the property and its fair market value. In the absence of the election, income, gain or loss, with respect to contributed property can be effectively shifted among members of the partnership. | The allocation of income, etc., with respect to contributed property would be made mandatory so that a partnership would generally have to allocate pre-contribution appreciation or depreciation to the contributing partner.<br><br>Effective date.--Contributions made after April 1, 1984.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>-- 0.1 0.1 0.2 0.4 | Effective date.--Contributions made after March 31, 1984. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| b. Allocations of partnership losses | The 1976 Act prohibited retroactive allocation of partnership deductions to partners entering late in the year by requiring each partner's various interests during the year to be taken into account in determining his distributive share of partnership items.<br><br>It may be possible to avoid the 1976 retroactive allocation rules through the use of tiered partnerships or, in the case of cash method partnerships, by delay of actual payments.<br><br>To the extent a loss allocated to a partner exceeds his basis in the partnership, the loss is not deductible. A limited partner's basis includes his share of non-recourse debt of the partnership. In Raphan v. U.S., the U.S. claims court treated as a nonrecourse debt of the partnership a debt guaranteed by the general partner as a third party. | In the case of cash basis partnerships and tiered partnerships, the Secretary would be required to provide methods for allocating partnership items among partners that take into account the varying interests of the partners during the taxable year.<br><br>For cash basis partnerships, certain items such as taxes, interest and rents would be allocated proportionately over the periods to which they relate, so that a partner could deduct only those items actually accrued while he was a partner.<br><br>Effective date.--Items paid or accrued after April 1, 1984.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>* * 0.1 0.1 0.2 | Also, reverse the holding in Raphan v. U.S.<br><br>Effective date.--Items paid or accrued after March 31, 1984. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| 2. Use of partnerships to convert character of income or to defer income<br><br>a. Character of gain or loss on contributed property | Present law provides that if certain ordinary income property of a partnership is distributed to a partner, its character as ordinary income property is preserved in the hands of the distributee for 5 years.<br><br>No comparable rule applies to property contributed to a partnership. Thus, it may be possible to change the character of property from ordinary income to capital gain or from capital loss to ordinary loss through a contribution to a partnership. | If unrealized receivables are contributed to a partnership, their ordinary income character would be preserved in the hands of the partnership.<br><br>If inventory is contributed to a partnership, its ordinary income character would be preserved in the hands of the partnership for 5 years.<br><br>Also, if a capital asset with a value less than its basis (i.e., a built-in loss) is contributed to a partnership, that loss would be treated as a capital loss if recognized by the partnership within 5 years.<br><br>Effective date.--Property contributed after April 1, 1984.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>* * 0.1 0.1 0.2 | Effective date.--Property contributed after March 31, 1984. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| b. Organizational fees and other capital expenditures | Generally, amounts expended to organize or promote a partnership must be capitalized. Other payments for property or service may also be required to be capitalized. These capitalization requirements may, in effect, be avoided when the payee is also a partner by allocating a greater share of gross income to that partner. | Provide that when a partner performs services for, or transfers property to, a partnership and receives a related allocation of partnership income or gain, the transaction will be treated as occurring between the partnership and a person who is not a partner. Thus, the amount of the allocation would be capitalized.<br><br>Effective date.--Services performed or property transferred after February 29, 1984.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>* * 0.1 0.1 0.1 | Effective date.--Date of Committee action. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| c. Disguised sales | A partner may avoid recognition of gain on the sale of property to his partnership or another partner by characterizing the transaction as a contribution of the property followed by a distribution of cash or other property to the partner. | Provide that a transfer of property to a partnership and a related transfer to the contributing partner would be treated as occurring between the partnership and a person who is not a partner and thus would be treated as a sale.<br><br>Effective date.--Transfers after April 1, 1984.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>* * * * * | Effective date.--Date of Committee action. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| d. Tiered Partnerships | Ordinary income property<br><br>Amounts received by a transferor partner in exchange for all or part of his partnership interest that are attributable to his interest in ordinary income assets of the partnership are treated as ordinary income.<br><br>If ordinary income assets are held in a second partnership in which the distributing partnership holds an interest, the rules characterizing income attributable to ordinary income assets may be avoided. | | Treat a partnership that own interests in another partnership as owning its proportionate share of the ordinary income assets directly. A similar rule would apply to interests in trusts.<br><br>Effective date.--Distributions, sales, or exchanges after March 31, 1984.<br><br>Revenue effect.--<br><br>NA |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| | Basis strips<br><br>Present law permits partnerships to elect to increase the basis of their assets by the amount of any basis that is "lost" when a distributee partner's basis in his interest is substituted for the basis of distributed property.<br><br>Thus, a partnership distributing high basis property to a low basis partner will experience an increase in the basis of its other property, but the distributee partner will lose basis and be exposed to be exposed to greater gain if the distributed property is sold.<br><br>This result can be avoided by contributing the high basis property to a lower tier partnership which has not elected to make basis adjustments on contributions, and by distributing the partnership interest to the low basis partner. The result is that the partnership property of the first partnership will experience a basis increase without reducing the basis in the contributed property. | | Eliminate the elective basis adjustment for distributions of interests in partnerships that have not elected to make basis adjustments.<br><br>Effective date.--Distributions after date of Committee action. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| 3. Like-kind exchanges of partnership interests | Present law permits like-kind exchanges of property held for productive use or investment to be made tax-free. These rules do not apply to inventory, stock, certificates of trust or beneficial interests, or other securities or evidences of indebtedness. In some cases, the courts have permitted tax-free like-kind exchanges of partnership interests. The Treasury has not acquiesced in these holdings. | Provide that tax-free like-kind exchange treatment is not available for exchanges of interests in different partnerships.<br><br>Effective date.--Exchanges after April 1, 1984, subject to binding contract exception.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>-- 0.2 0.6 0.7 1.5 | Effective date.--Exchanges after March 31, 1984, subject to a binding contract exception. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| 4. Transactions in mutual fund shares | Mutual fund distributions from capital gain income are taxed as long-term capital gain to its shareholders even when made to a shareholder who has held the share for one year or less.<br><br>If a shareholder who has held the share less than 31 days sells his shares in the mutual fund at a loss after a capital gain dividend has been received, the loss is treated as long-term rather than short-term to the extent of the capital gain dividend. Similar rules apply to real estate investment trusts. | Losses on stock held for 6 months or less would be treated as long-term losses to the extent of any capital gain dividends paid on the stock. There would be an exception for periodic redemption plans.<br><br>Effective date.--Losses with respect to holding periods beginning after enactment.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>-- -- .1 .1 .2 | |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| 5. Multiple trusts | Grantors of trusts may reduce present taxation by establishing multiple trusts for the same beneficiaries which take advantage of the separate graduated rate applying to each trust. | | Trusts established by the same grantors for substantially the same beneficiaries with a principal purpose of tax avoidance would be consolidated for tax purposes under Treasury regulations.<br><br>Effective date.--Taxable years beginning after Committee action.<br><br>Revenue effect.-- |
| 6. Trusts distributions | Beneficiaries are taxed on amounts distributed from a trust (or estate) to the extent of the trust's (or estate's) distributible net income. The trust (or estate) is allowed a deduction for amounts taxed to its beneficiaries.<br><br>Distributions of appreciated property are deemed to carry out distributable net income to the extent of the property's value at the time of distribution. The basis of the property in the hands of the beneficiary is its value to the extent it carries out distributable net income. | | Distributions of property would carry out distributable net income only to the extent of the property's basis. Accordingly, the beneficiary's basis would be the same as the trusts' (or estate's) and the appreciation would no longer be exempted from tax.<br><br>Effective date.--Distributions after date of Committee action.<br><br>Revenue effect.--<br><br>NA |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| 6. Trusts distributions (Cont.) | Under these rules, distributions of appreciated property result in exemption of the appreciation from tax to the extent that the trust (or estate) has distributable net income. | | |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| 1. Dividends Received by Corporations<br><br>a. Debt-financed portfolio stock | When a corporation borrows the funds used to purchase dividend-paying stock, interest on the acquisition indebtedness is generally deductible against ordinary income. Dividends received by a corporation are eligible for an 85-percent dividend received deduction. Thus, a corporation that borrows to finance purchases of portfolio stock effectively converts ordinary income to dividend income which is taxed at a maximum rate of 6.9 percent. | The deduction for interest on debt incurred by a corporation that is directly attributable to an investment in stock would be disallowed in an amount equal to the dividends received deduction on the leveraged stock.<br><br>Effective date.--Leveraged stock investments entered into after the date of enactment.<br><br>Revenue effect.<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>* * * * * | |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| b. Extraordinary dividends received by corporations | Dividends received by a corporation generally have no effect on its basis in the stock of the distributing corporation. As a result, a corporation can buy stock for $100, receive a $15 extraordinary dividend on it, and then in short order sell the stock for $85. While some portion (generally 15 percent) of the $15 dividend will be taxed as ordinary income to the recipient corporation, the transaction, which has no economic consequences, will also generate $15 of short-term capital loss on the sale of the stock. This is an attractive transaction for corporations that have capital gains which can be sheltered by the loss on the sale of stock. | If a corporate shareholder does not hold stock for at least one year, the fair market value of any extrordinary dividend (to the extent not subject to tax) would reduce its basis in the stock. Extraordinary dividends would include dividends received within any 90-day period with a fair market value equal to or greater than 10 percent (five percent in the case of preferred stock) of the taxpayer's basis in the stock. Extraordinary dividends would also include dividends received within any one-year period with a fair market value equal to or greater than 20 percent of the taxpayer's basis in the stock (common or preferred). | An exception for non-deep-in-the money covered calls could be made for purposes of the holding period rule. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| | | The one-year holding period (as well as the 15-day and 90-day periods under present law) would be limited to exclude any period during which the taxpayer is grantor of an in-the-money option with respect to the stock, or any period that the taxpayer's risk of loss is substantially diminished because of holding other positions. A corporate shareholder's holding period for property received as a dividend could not exceed its holding period for its stock in the distributing corporation.<br><br>Effective date.--Stock positions acquired after date of enactment.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>* .1 .1 .2 | The basis adjustment could be effective for distributions made after date of Committee action. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| c. Certain dividends received from regulated investment companies | A regulated investment company (RIC) is not subject to Federal income tax to the extent it distributes its income to shareholders. If at least 75 percent of a RIC's gross income consists of dividends from domestic corporations, then the entire amount of the RIC's dividends to its shareholders is eligible for the 85-percent intercorporate dividends-received deduction (sec. 854). Taxpayers have organized RICs, expressly for corporate investors, to take advantage of the tax provision that permits the pass-through of interest income (taxable at a maximum rate of 46 percent) to corporations as tax-favored dividend income (the maximum rate on which is only 6.9 percent). | | The 75-percent rule of present law could be raised to 100 percent for corporate shareholders.<br><br>Effective date.--Taxable years after date of enactment.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>* .1 .1 .2 |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| d. Dividends received deduction compliance | A broker who holds stock in street name for a customer may lend that stock to another customer for use in a short sale. The short-seller sells the borrowed stock with the expectation that the price of the stock will decline and expects to be able to purchase stock to return to the lending broker at a price below the proceeds of the sale. If a dividend is paid on the borrowed stock, the short-seller must pay the lender an amount in lieu of the dividend. The actual dividend is received by the purchaser in the short sale. If the borrowed stock belonged to a corporate client of the broker, the corporation is not entitled to the dividends received deduction on the amount of the payment received in lieu of the dividend. | | The broker reporting rules would be amended to require brokers to provide a statement to corporate customers of amounts paid in lieu of dividends by reason of short sales.<br><br>Effective date.--January 1, 1985.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>* * * * * |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| 2. Ordinary nonliquidating dividends of appreciated property (including royalty trusts). | Generally, a distribution of appreciated property by a corporation with respect to its stock is not a taxable event to the distributing corporation. As an exception to the general nonrecognition rule, however, taxable gain is recognized to the distributing corporation on distributions of appreciated property in certain redemptions. Distributions of appreciated property in regular dividend transactions generally are not taxable events to the distributing corporation. | Any ordinary, nonliquidating distribution of appreciated property to a noncorporate shareholder would be taxable to the distributing corporations. Certain exceptions of present law (relating to, among other things, partial liquidations, carryover basis situations, and distributions of qualifying stock) would remain.<br><br>Effective date.--Distributions after the date of enactment with a transition rule to exclude transactions substantially underway on February 1, 1984.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>* * .1 .1 .2 | |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| 3. Investment companies that accumulate earnings | A corporation may deduct 85 percent of the dividends it receives on portfolio stock investments. Furthermore, gain on the sale of stock held by an individual for more than one year is generally taxed as long-term capital gains at rates not in excess of 20 percent.<br><br>As a result, an investment company can be set up to be widely-held by individual investors and to invest in dividend-paying stocks. The investment company itself would pay no dividends. Rather, its shareholders would hold the stock for at least a year and then sell it at a price that reflects dividends received and retained by the company. Their gains would generally be long-term capital gain, so individual shareholders would essentially be recognizing dividend income at a tax rate substantially below 50 percent. The company may take the position that it is not subject to the accumulated earnings tax because it is widely-held, an argument some courts have embraced in other contexts. | It would be made clear that the mere fact that a company is widely held does not exempt it from the accumulated earnings tax. Also, the net capital loss deduction would be denied for mere investment or holding companies.<br><br>Effective date.--Taxable years beginning after the date of enactment.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>.1 .1 * .2 | |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| 4. Expenses incurred in connection with short sales | A short sale is a transaction in which the investor borrows stock, sells the stock and later buys stock to repay the loan. Amounts paid by the taxpayer to the lender in lieu of dividends are deductible against ordinary income. A taxpayer can create short-term capital gain and ordinary loss by selling short before a dividend payment date and closing the short sale after the dividend date in a transaction with essentially no economic consequences. | In the case of a short sale of stock, payments in lieu of dividends would not be deductible against ordinary income unless the short sale is held open for at least 16 days. No deduction would be allowed for payments in lieu of extrordinary dividends, unless the short sale is held open for at least one year. The disallowance amounts would be treated as part of the basis of the short seller in the stock acquired to close the short sale.<br><br>Effective date.--Short sales opened after the date of enactment.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>* * * * .1 | |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 5. Transfers of partnership interests by corporations | When a partnership interest is sold, any gain is ordinary income to the extent attributable to certain ordinary income items of the partnership. When a corporation distributes property, or sells property in the course of certain complete liquidations, recapture income is taxed to the corporation while non-recapture gain attributable to appreciation in the transferred property goes unrecognized. However, it has been argued that the corporate recapture provisions do not apply to the distribution of an interest in a partnership that holds recapture property.<br><br>Thus, taxpayers have argued that to avoid recapture, a corporation may contribute recapture property to a partnership and distribute the partnership interest to its shareholders, or sell it in the course of liquidation. | A corporate distribution or a liquidating sale of a partnership interest would be treated as a transfer of the distributing corporation's allocable share of certain recapture items held by the partnership. The amount of income recognized would be limited to the gain the corporation would have recognized had it sold the partnership interest.<br><br>Effective date.--Dispositions after April 1, 1984.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>* .1 .1 .1 .2 | The effective date could be the date of Committee action. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 6. Transactions involving foreign corporations<br><br>a. Certain transfers of appreciated property to foreign corporations | Under section 367, certain transfers of appreciated assets to foreign corporations in reorganizations and liquidations, which would be tax-free, are taxable if the Internal Revenue Service rules that one of the principal purposes of the transfers was the avoidance of Federal income tax. Under Internal Revenue Service guidelines, generally, transfers of property used in the active conduct of a foreign trade or business are not taxed. However, also under those guidelines, transfers of assets containing built-in gain (such as inventory and accounts receivable) are generally taxed.<br><br>Judicial interpretation of the principal purpose test has reduced the ability of the Internal Revenue Service to administer section 367. In addition, the Internal Revenue Service's current ruling policy permits the tax-free transfer of intangible property abroad, where the development of the property generated significant U.S. tax | The rules governing transfers of appreciated property abroad would be amended to provide for gain recognition without regard to purpose, unless the property is transferred for use in an active trade or business abroad. Certain transfers of assets containing built-in gain would automatically be subject to tax. Transfers of stock would be subject to the active trade or business test. In addition, transfers of intangibles for less than full consideration would be subject to tax. Full consideration would include an arm's length royalty. Finally, the current Internal Revenue Service policy on incorporations of foreign branches could be codified.<br><br>Effective date.--Transfers after July 1, 1985.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1985 1986 1987 84-87<br>-- * .1 .1 | The provision could be made effective January 1, 1985. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| Certain transfers of appreciated property to foreign corporations | benefits but the income derived from the property may escape U.S. taxation. Finally, the courts have rejected the Internal Revenue Service's requirement that certain losses be recaptured upon the incorporation of a foreign branch by a U.S. person. | | |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| b. Decontrol of foreign corporations | Under section 1248, when a U.S. taxpayer who is a 10-percent shareholder of a controlled foreign corporation sells or exchanges stock in a taxable transaction, the gain is treated as ordinary (dividend) income to the extent of the shareholder's pro rata share of the corporation's post-1962 accumulated earnings and profits. A U.S. corporation that disposes of stock by distributing it as a dividend-in-kind or in the course of liquidation, in a transaction eligible for nonrecognition treatment to the U.S. corporation, is also required to include in income its share of post-1962 accumulated earnings and profits. Taxpayers have taken the position that section 1248 does not apply if a controlled foreign corporation that is wholly owned by a U.S. corporation issues new shares for shares of the U.S. corporation. If this position were sustained, such a transaction could lead to permanent exemption from U.S. corporate tax of the earnings of the controlled foreign corporation accumulated prior to the exchange. | Certain exchanges by a controlled foreign corporation of its newly issued stock for shares of its U.S. parent corporation would be treated as a sale or exchange by the U.S. parent of stock in the controlled foreign corporation.<br><br>Effective date.--Date of enactment.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>* * * * * | |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| c. Recharacterization of U.S. income as foreign income | The United States insists on taxing the "U.S. income" of U.S. taxpayers. U.S. taxpayers' "foreign income" can be free of U.S. tax, under the foreign tax credit. U.S. taxpayers can place the "foreign" label on some U.S. income (such as interest and insurance premiums) by routing it through a foreign corporation. This foreign corporation distributes "foreign" dividends to its U.S. owners. This newly "foreign" income may escape U.S. (or foreign) tax. | | The proposal would prevent re-labelling of U.S. income as foreign. If a corporation, 10 percent (or more) of whose gross income is U.S. income (including U.S. business income), pays interest or dividends to a U.S. taxpayer, a pro rata portion of the payment would be U.S. income. Thus, if 75 percent of a corporation's gross income is U.S. income (over a three-year period), 75 percent of the dividends and interest it pays U.S. income. It would apply only to 50-percent U.S.-owned corporations.<br><br>Effective date.--The proposal would apply to income earned by paying corporations after date of enactment.<br><br>Revenue effect.--<br><br>NA |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| d. Recharacterization of interest income as dividend income | A U.S. taxpayer's foreign interest income cannot escape both U.S. and foreign tax (under the United States' separate foreign tax credit limitation that prevents foreign taxes on non-interest income from offsetting U.S. tax on foreign interest income). U.S. taxpayers seek to circumvent this rule by creating foreign subsidiaries to earn foreign interest income (for example, by depositing money in foreign banks). When the U.S. taxpayer is taxable on the earnings of its foreign subsidiary, its income is dividend income, not interest income. Thus, newly recharacterized "non-interest" income may totally escape both U.S. and foreign tax. | | The committee could treat foreign dividends as interest to the extent that the paying corporation's earnings and profits arise from interest. This rule would apply only if 10 percent or more of the paying corporation's earnings and profits arise from interest. It would apply only to 50-percent U.S.-owned corporations.<br><br>Effective date.--The proposal would apply to income earned by paying corporations after the date of enactment.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>* * * .1 .1 |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| e. Use of territories to avoid U.S. tax on foreign investors | Payments of U.S. source interest, dividends, and other passive income to foreign investors are generally subject to a 30-percent U.S. withholding tax. The United States does not tax payments of passive income to corporations organized in Guam, the Northern Mariana Islands, or the U.S. Virgin Islands. Some argue that foreigners who wish to invest in the United States may avoid both U.S. and territorial tax by channeling their investments through conduit corporations in these territories.<br><br>Temporary Treasury regulations subject dividends and interest paid by territorial conduit corporations to territorial withholding tax. Guam is contesting these regulations in court. | | Interest, dividends, and other passive income paid from U.S. sources to corporations organized in Guam, the Marianas, or the Virgin Islands could be subject to U.S. tax unless the bulk of the recipient's gross income is from its territory and unless the bulk of its beneficial owners are local residents.<br><br>Effective date.--Payments after date of Committee action.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>* * * .1 .2 |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| f. Source of shipping income | In general, the United States taxes all U.S. income, but not all foreign income, of United States persons. In general, the United States does not tax the foreign income of non-United States persons (such as foreign corporations). Under present law, shipping income can be almost all foreign even if the voyage is between two U.S. ports or a U.S. port and a foreign port. | | Income earned for transportation that begins and ends in the United States (or U.S. possessions) would be U.S. income. Transportation includes services income and leasing income. It includes income from ships, airplanes, and containers.<br><br>Effective date.--Date of enactment.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>* * .1 .1 .2 |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| g. Foreign collapsible corporations | Sales of inventory yield ordinary income, not capital gain. "Collapsible" corporations' assets generally include inventory. Generally, a shareholder's gain on the sale or liquidation of a collapsible corporation is ordinary income rather than capital gain. However, if a collapsible corporation consents to recognize ordinary income on disposition of its inventory and the like, the shareholder gets capital gain treatment on the sale or liquidation of the corporation.<br><br>Some take the position that a foreign corporation can give consent to recognize ordinary income. If so, enforcement of the consent is impractical. | | The committee could require U.S. shareholders to pay tax at ordinary income rates on disposition of a foreign collapsible corporation. That is, disregard any consents of foreign corporations to recognize ordinary income on disposition of noncapital assets.<br><br>Effective date.--Date of enactment.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>* * * * * |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 7. Transactions in stock warrants | Present law is unclear as to the tax consequences of dealing a corporation's own warrants. A corporation dealing in its own stock does not recognize gain or loss. Under present law, taxpayers with a gain may take the position that no gain is recognized and taxpayers with a loss may report the loss. | | It could be provided that no gain or loss is recognized by a corporation on any transaction with respect to a warrant to buy or sell its own stock.<br><br>Effective date.--Warrants acquired or lapsed after date of enactment.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1985 1987 84-87<br>* * * * * |
| 8. Exchange of debt for stock | Under present law a corporation recognizes gain when it buys back its debt at less than par value. The gain may be deferred. However, a corporation does not recognize gain when the debt is repurchased by issuing its own stock. Thus a corporation is treated differently where it raises cash to discharge its debts by issuing new stock and where it discharges the stock by issuing stock directly. | | It could be provided that the scope of the "stock for debt" exception be limited to insolvent or bankrupt corporations.<br><br>Effective date.--Transfers after date of enactment.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>NA |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 9. Distribution of debt by a corporation--Earnings & Profits | Earnings and profits of a corporation are reduced by the principal amount of its obligations distributed to shareholders. Generally, for noncorporate shareholders, the amount of a distribution taken into account is the fair market value of the property distributed. A long-term obligation bearing little or no stated interest may have a present fair market value well below its stated redemption price. The result may be to eliminate corporate earnings and profits at the cost of a relatively small dividend to shareholders. | | The earnings and profits rules could be amended to provide that earnings and profits are reduced only to the extent of the fair market value of the corporation's debt distributed to its shareholders. Also such obligations could be made subject to the original issue discount rules.<br><br>Effective date.--Distributions after date of enactment.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>(Billions of Dollars)<br><br>1984 1985 1986 1987 84-87<br><br>Not available. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 10. Definition of affiliated group of corporations | Present law allows an affiliated group of corporations to file a consolidated return. For certain tax rules, an affiliated group of corporations is treated as a single corporation. Affiliation can be achieved even though convertible preferred stock with a significant equity value is owned by outsiders. Furthermore, affiliation can be avoided by the issuance of non-voting common stock having a small equity value to outsiders. | | The definition of "affiliated group" (section 1504(a)) could be amended to require 80 percent of the equity as well as 80 percent of the voting power in order to consolidate.<br><br>Effective date.--Taxable years beginning after December 31, 1984 with appropriate transitional rules. |

## D. TIME VALUE OF MONEY AND OTHER ACCOUNTING ISSUES

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| 1. Deferred payment transactions<br><br>(a) Time for inclusion or deduction of deferred interest. | In general, in a discount lending transaction (where all or a portion of the interest is not payable currently), the borrower is treated as having paid, and the lender as having received, the annual unpaid interest, which was then relent to the borrower. This matches the interest inclusion by the lender with the interest deduction by the borrower. The original issue discount (OID) rules do not apply to obligations issued in exchange for property where neither the obligation nor the property is publicly traded; to obligations issued by individuals; as to holders of discount obligations, to obligations not held as capital assets; or to deferred payments for services or use of property. | Extend the OID rules to obligations issued for nontraded property, issued for services or use of property, issued by individuals, and not held as capital assets. The interest element in obligations issued for nontraded property, services, or use of property would be compared to a test rate. The test (safe harbor) rate would be 120 percent of an average yield on Federal obligations of similar maturity (the "applicable Federal rate"). This yield would be redetermined semiannually for 3 categories of maturities (short-, medium-, and long-term). If interest were not paid at least at this rate, interest would be imputed at a rate equal to 130 percent of the applicable Federal rate and annually included in the income of the lender and deducted by the borrower. The Secretary would be authorized to require any lender disposing of an OID obligation within these rules to provide adequate information such that the transferee could determine his taxable income. Exceptions to these rules would be provided for sale of principal residences, certain sales of farms, and sales involving total payments of $250,000 or less.<br><br>Effective date.--Transactions entered into after December 31, 1984. | Apply a test rate equal to 110 percent of the applicable Federal rate, and impute interest at a rate of 120 percent of the Federal rate if the test rate is not satisfied.<br><br>Clarify application of OID with respect to nonresident aliens. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| (b) Measurement of interest in deferred payment transactions. | If the parties to a deferred payment sale fail to state interest at a safe-harbor rate fixed by regulation, interest is imputed at a higher rate fixed by regulation. The safe-harbor rate is a simple interest rate; the imputed rate is a compound rate. Imputed interest is allocated among deferred payments in proportion to the amount of the payment, without regard to the period of time that has elapsed since the sale. | The adequacy of the interest element in a deferred payment sale would be tested against a self-adjusting compound rate of interest which approximates a market rate. This test (safe-harbor) rate would be the same rate applied under the proposed amendments to the OID rules: 120 percent of the applicable Federal rate. If insufficient interest were stated, interest would be imputed at a rate equal to 130 percent of the applicable Federal rate. Interest income would be recognized by the lender and interest expense would be deducted by the borrower on an economic accrual basis according to the taxpayer's normal method of accounting.<br><br>Effective date.--Transactions entered into after December 31, 1984.<br><br>Revenue effect.<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 .2 / 1985 .6 / 1986 1.0 / 1987 1.4 / 84-87 3.2 | Provide a safe harbor rate of 110 percent of the applicable Federal rate and an imputed rate of 120 percent of the applicable Federal rate.<br><br>Effective date.--The changes requiring computation of interest on a compound basis and which allocate interest to payments on an economic accrual basis would apply to transactions entered into after the date of Committee action, except those subject to a binding commitment on that date. The changes to the safe-harbor and imputed interest rates would apply to transactions entered into after December 31, 1984. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 2. Premature accruals | Under the accrual method of accounting, an expense is deductible when--<br><br>(1) all events have occurred the fact of liability, and<br><br>(2) the amount of the liability can be estimated with reasonable accuracy.<br><br>The proper time for deducting expenses for which economic performance has not yet occurred is the subject of controversy under present law. | Require that economic performance must occur before all events establishing the fact of liability will be considered to have occurred.<br><br>Exceptions.--Items for which specific timing rules are provided under the Code, such as bad debts and vacation pay.<br><br>NOL carrybacks.--Provide a 10-year carryback for losses arising from certain deferred liabilities (or, if earlier, to the year decommissioning liability arose in the case of nuclear power facilities).<br><br>Effective date.--Expenses accruing after date of enactment.<br><br>Revenue effect.<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br><br>.3 .6 .6 .6 2.2 | |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 3. Prepaid expenses | Except with respect to interest and prepayments by farm syndicates, present law is unclear as to the proper timing of a deduction for prepaid items by cash method taxpayers.<br><br>In the case of interest, deductions are allowed only for the year to which the interest relates. A similar rule applies to prepaid expenses of farm syndicates. | Tax shelter organizations would not be permitted to deduct any amount prior to the time it would be properly deductible under the accrual method of accounting.<br><br>Tax shelter organizations would be--<br><br>(1) partnerships and other entities (other than regular corporations) interests in which are offered for sale in a registered offering;<br><br>(2) partnerships or other enterprises in which more than 35 percent of the losses are allocated to limited partners or limited entrepreneurs (for this purpose, individuals who have actively participated in the management of the enterprise would not be treated as limited partners or entrepreneurs); and<br><br>(3) any entity, plan or arrangement having the principal purpose of tax avoidance or evasion.<br><br>Effective date.--Prepayments after date of enactment.<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>.1 .3 .1 .1 0.6 | |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 4. Deferred like-kind exchanges. | No gain or loss is recognized on the exchange of business or investment property for property of like-kind.<br><br>Under the case law, an intended like-kind exchange transaction may be held open for as much as 5 years. | Property received more than 90 days after the taxpayer transfers the relinquished property would not be treated as like-kind property.<br><br>Effective date.--Transfers of property after date of enactment.<br><br>Revenue effect.<br><br>Fiscal Years, 1984-87<br><br>1984 1985 1986 1987 84-87<br>.1 .1 .1 .1 .5 | The 90-day period could be extended to 180 days (but not beyond the due date for the return). |
| 5. LIFO conformity | The "Last-In-First Out" (LIFO) method of inventory accounting may not be used for tax purposes unless it is also used in reporting to shareholders, partners, other proprietors, beneficiaries, or for credit purposes. An issue has arisen as to whether a parent company is subject to the LIFO conformity rules when the inventory is held by a subsidiary company. | Apply the LIFO conformity requirement to a controlled group of corporations.<br><br>Effective date.--Taxable years beginning after date of enactment.<br><br>Revenue effect.<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>-- .1 .2 .2 .5 | |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 6. Inclusion of tax benefit items in income | An individual taxpayer who receives a State tax refund may exclude from income the excess of the zero bracket amount over the taxpayer's other itemized deductions for the year in which the State taxes were deducted. This exclusion is permitted even though the deduction of this amount in the prior year resulted in a tax benefit. | | Provide that where a taxpayer recovers a previously-deducted amount, the recovered amount is excluded from gross income only to the extent such amount did not reduce income subject to tax.<br><br>Effective date.--Amounts recovered after December 31, 1983.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars] |
| 7. Below market-interest and interest-free loans | Loans between family members generally result in taxable gifts in an amount equal to the value of the interest that is not charged. No income tax consequences result, however, to either the lender or the borrower. Loans by corporations to their shareholders, and loans to persons providing services by persons for whom the services are provided generally do not have any Federal tax consequences. | Low-interest and interest-free loans would be recharacterized as (1) a loan to the borrower at a statutory interest rate, and (2) either a gift (in the case of a family transaction), dividend (in a corporation-shareholder transaction), or compensation (in a transaction involving services). The borrower would be treated as paying interest on the loan at the statutory rate, resulting in income to the lender and a deduction to the borrower. The Secretary would be directed to issue regulations providing exceptions for non-tax motivated transactions. | |

| 1984 | 1985 | 1986 | 1987 | 84-87 |
|---|---|---|---|---|
| -- | 0.2 | 0.3 | 0.3 | 0.8 |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| | | Effective date.--Date of committee action (other than demand loans repaid within 60 days of such date).<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>* .1 .1 .1 .3 | |
| 8. Income averaging | Income averaging is available to taxpayers with "averageable income". Averageable income is current year taxable income in excess of 120 percent of average taxable income in the 4 preceding years.<br><br>In effect, income averaging widens the tax brackets by a factor of five with respect to averageable income. | | The 120-percent requirement could be increased to 140 percent and only the three prior years taken into account.<br><br>Income averaging would be modified so that it, in effect, widens the tax brackets by a factor of four, not five, with respect to averageable income.<br><br>Effective date.--Taxable years beginning after December 31, 1983.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br><br>1984 1985 1986 1987 84-87<br>.1 2.0 1.9 2.1 6.1 |

## E. DEBT OBLIGATIONS ACQUIRED AT A DISCOUNT

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| 1. Debt obligations acquired at a discount<br><br>a. Market discount | Market discount serves as a substitute for coupon interest. However, upon the disposition of a market-discount bond issued by a corporation or a governmental unit and held for more than one year, capital gain treatment is accorded to the appreciation in value attributable to market discount. When a taxpayer borrows the funds used to purchase a market-discount bond, interest on the acquisition indebtedness generally can be deducted currently against ordinary income. Thus, a taxpayer who leverages the purchase of a market-discount bond effectively converts ordinary income to capital gain. | Gain on the redemption or sale of a market-discount bond would be recognized as interest income to the extent of accrued market discount. Taxpayers could elect to accrue the discount under an economic accrual formula or under a less complex, but also less generous, linear formula. The proposal would not apply to tax-exempt obligations.<br><br>Effective date.--Bonds issued on or after date of enactment.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>(Billions of Dollars)<br><br>1984 1985 1986 1987 84-87<br><br>* * * * * | Interest deductions allocable to indebtedness incurred to purchase or carry a market-discount bond would be deferred, to the extent such interest exceeds interest income from the bonds.<br><br>Effective date.--Obligations acquired after date of enactment.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>(Billions of Dollars)<br><br>1984 1985 1986 1987 84-87<br><br>0.2 0.7 0.1 0.1 1.0<br><br>Note: This estimate represents the combined effects of this proposal as well as the proposal G-1(c) concerning short-term obligations issued at a discount. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| b. Zero coupon municipal bonds | Original issue discount on noninterest-bearing obligations issued by a municipality is exempt from tax under the general rule of section 103(a). Under Internal Revenue Service rulings, tax-exempt original issue discount is apportioned ratably among the original holder and subsequent purchasers of a bond. The application of this rule permits the holder of a zero coupon municipal bond to generate an artificial loss by disposing of the bond prior to maturity. | No proposal. | Tax-exempt original issue discount would be accrued under an economic accrual formula. The holder of a zero coupon municipal bond would receive a basis adjustment to reflect the economic accrual of the discount.<br><br>Effective date.--Obligations issued after September 3, 1982 (date of enactment of TEFRA) and acquired after date of Committee action.<br><br>Revenue effect.<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br><br>* * * * * |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| c. Certain short-term obligations issued at a discount | For governmental obligations (Treasury bills) issued at a discount and payable without interest at a fixed maturity not exceeding one year, the acquisition discount is not considered to accrue until the obligation is paid at maturity or otherwise disposed of. This rule applies regardless of whether the taxpayer uses the accrual or the cash method of accounting. A similar rule applies to cash-basis taxpayers who hold other obligations with a maturity of one year or less (e.g., bank certificates of deposit). Taxpayers who make leveraged purchases of obligations eligible for the special rules are able to defer tax liability on unrelated income. | No proposal. | To deal with leveraged purchases of short-term discount obligations, interest deductions on indebtedness incurred to purchase or carry such obligations would be deferred until the interest on the obligations is included in income.<br><br>The committee may also wish to review the scope of the provision that permits tax deferral on Treasury bills. Under present law, tax deferral is available to all taxpayers. One possibility would be to require accrual-basis taxpayers and cash-basis taxpayers who acquire Treasury bills in the course of a trade or business to account for the acquisition discount on the accrual basis, regardless of whether the Treasury bill is debt-financed. If this rule were adopted, taxpayers could be permitted to spread the payment of any net tax liability over a 10 year period.<br><br>Effective date.--Obligations acquired after date of enactment.<br><br>Revenue effect.--<br>See item G-1(a). |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 2. Income from factoring trade receivables | A seller who sells goods for the buyer's receivable (a transferable debt) may sell that receivable to a third party--a factor--at a discount. If a U.S.-owned factor is in a tax haven, it may earn income free of U.S. tax. That income may be eligible for deferral, and it may be foreign-source income that is sheltered by excess foreign tax credits.<br><br>When a foreign subsidiary of a U.S. corporation invests in U.S. property (for example, by lending funds to its U.S. parent), that investment is taxable as a dividend to the U.S. parent. Some taxpayers allege that this rule does not apply to a foreign factoring subsidiary that buys receivables from its U.S. parent. | When a foreign factoring subsidiary of a U.S. owner gets cash for a receivable that (1) it bought from a related person, and (2) the related person had taken in exchange for inventory, tax the U.S. owner on that factoring income. Treat income from a related U.S. person's receivables as U.S. income.<br><br>Treat payments of cash from a foreign subsidiary to a related U.S. person for receivables arising from the U.S. person's sales of inventory as investments in U.S. property. Thus, payments of cash for receivables would be taxable as dividends to the U.S. parent.<br><br>Effective date.--Transfers after date of Committee action.<br><br>Revenue effect.<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br><br>* 0.1 0.2 0.3 0.7 | |

## F. COMPLIANCE PROVISIONS

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| 1. Promoter's customer lists | Promoters of tax-oriented investments are not required to keep customer lists available to the IRS. | None. | Require promoters of investments that offer tax representations to maintain customer lists in the manner provided by Treasury regulations.<br><br>Penalty.--$50 per failure to list a customer up to $50,000 per year.<br><br>Effective date.--date of enactment. |
| 2. Promoter penalty | TEFRA provided for a penalty on promoters of abusive tax shelters equal to the greater of--<br>$1,000, or<br>10 percent of income from the activity. | None. | Increase the 10-percent penalty to 20 percent.<br><br>Effective date.--Day after the date of enactment. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 3. Practice of Appraisers | The Treasury has no authority to prevent disreputable appraisers from providing appraisals for use on tax returns or from appearing in proceedings before the Treasury. | None. | Provide that the Treasury may bar appraisers who aid or assist in the preparation of false returns or other documents from practice before the Treasury.<br><br>Effective date.--Date of enactment. |
| 4. Foreclosure reporting | Foreclosures in satisfaction of a debt or forgiveness of a debt may give rise to income to the debtor which may be treated as ordinary income under the recapture rules. | None. | Require persons lending in the course of a trade or business to report to the IRS when there is a foreclosure, satisfaction of the debt by acquisition of property, or an abandonment of security for a loan. (97)<br><br>Penalties.--Same as for other information returns (generally $50 per failure).<br><br>Effective date.--Foreclosures, etc., after December 31, 1984. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 5. Mortgage interest reporting | No informational reports are required with respect to amounts deductible by individual taxpayers who itemize their deductions. | None. | Require persons (including governmental units) who receive mortgage interest payments in the course of a trade or business to report annually to the IRS the amount of the interest, and the person from whom the payment is received. The payor would have to be provided a copy of the report. Payments aggregating less than $600 would be exempt.<br><br>Penalties.--Same as those for other information returns (generally $50 per failure).<br><br>Effective date.--Payments after December 31, 1984. |
| 6. Sales or exchanges of partnership interests | When a partnership interest is sold or exchanged, the transferred partner may have reportable gain or loss. In addition, if the value received is attributable to appreciated inventory or unrealized receivables that could produce ordinary income if sold by the partnership, the transferor will be treated as having realized ordinary income. | None. | When partnership interests are sold or exchanged, require the partnership to inform the IRS, the seller and the buyer of the fair market value of the allocable share of unrealized receivables and inventory.<br><br>Penalties.--Same as for the information returns (generally $50 per failure).<br><br>Effective date.--Sales or exchanges after December 31, 1984. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 7. IRA reporting | An individual generally may deduct the amount of qualified IRA contributions made for a year, either during the year or before the due date of the income tax return for the year. In the absence of reporting by the trustee or issuer, the IRS has difficulty verifying whether contributions were made and the year to which they relate. | None. | Clarify the authority of the Treasury to require reporting on contributions to IRAs by the trustee or issuer. Reports would include amount and year to which contribution relates.<br><br>Penalties.--Same as for other information returns (generally $50 per failure).<br><br>Effective date.--Contributions made after April 15, 1984, and relating to 1984 and subsequent years. |
| 8. Reporting of State income tax refunds | State and local governments are required to provide information to the IRS on refunds of State or local income tax, and to supply a copy to the taxpayer in January of the following year.<br><br>Under temporary regulations, the Treasury has provided that reporting is not required when the officer making the refund determines that that individual received no Federal tax benefit from the tax payment to which the refund relates. | None. | Codify the provisions of the temporary regulations providing exceptions from the reporting requirement.<br><br>Effective date.--Refunds and credits and offsets allowed after December 31, 1982. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 9. Revenue effect of compliance provisions | | | The proposals in items 1-9 would increase revenues by<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>-- * 0.1 0.2 0.3 |

## G. EMPLOYER-EMPLOYEE ITEMS

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| 1. Welfare Benefit Plans<br><br>a. Employer deductions | Generally, an employer's contribution to a fund which is part of a welfare benefit plan is deductible in the year the contribution is made, even though the benefits for which the contribution is used may not be paid to the employee for many years. This is similar to the tax treatment of contributions to a qualified pension plan, which is subject to many more requirements than a welfare plan. Contributions for post-retirement medical benefits of qualified plans are not taken into account in computing whether benefits under those plans satisfy the prescribed limits. An accrual method taxpayer may accrue vacation pay that is payable before the close of the succeeding taxable year, even though it will not be paid until a much later year. | | Generally, an employer's deduction for a contribution to a funded welfare benefit plan would be allowed at the same time and in the same amount as if the benefit were provided directly by the employer under an unfunded plan. In addition, for certain insurance-type benefits, a deduction would be allowed for an addition to a reserve, which generally would be limited to 50 percent of the average annual payments for these benefits during the past 3 years; higher reserves would be allowed in certain cases. Contributions for post-retirement medical benefits provided under a qualified pension plan to owners of more than 5 percent of the employer would be considered as a plan contri- for purposes of applying the limits. An accrual method taxpayer could deduct the amount necessary so that its vacation pay account is the amount reasonably expected to be paid before the end of the succeeding year.<br><br>Effective date.--Contributions made after March 31, 1984. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 1. Welfare Benefit Plans (cont.)<br><br>b. Tax-exempt funding | A tax-exempt supplemental unemployment benefit trust or voluntary employees' beneficiary association (VEBA) may be established and maintained by an employer as a funding medium for welfare benefits. Traditionally, VEBAs have been used by employee organizations to provide life, health, accident, disability, and unemployment benefits and to provide customary recreational facilities. A VEBA may not be used by an employer to fund deferred compensation, but VEBAs have been used recently to accumulate deductible funds set aside to provide severance pay to the operator of a professional corporation. | | The rules providing for benefits permitted to be paid from a VEBA would be clarified to exclude deferred compensation benefits essentially equivalent to wages. The rules requiring notice to the IRS of a claim of exempt status for a benefit organization would be clarified. The investment income of a benefit organization would be subject to the tax on unrelated business income to the extent assets exceed permitted levels, and contributions of property from an employer to a related exempt benefit organization would be treated as a transaction between related parties.<br><br>Effective date.--Taxable years beginning after December 31, 1984. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 1. Welfare Benefit Plans (cont.) | | | |
| c. Discrimination rules for plans of exempt benefit organizations | A VEBA is subject to standards that forbid discrimination in favor of employees who are officers, shareholders, or highly compensated. The rules are not clearly defined. | | The rules prohibiting discrimination would be clarified. If a benefit is of a type for which nondiscrimination is required as a condition of an exclusion of gross income, the exempt organization could provide the benefit only if the benefit conforms to the specified standard. Other benefits could not discriminate in favor of highly compensated employees as to eligibility or benefit level. Also, a benefit for highly-paid, etc., employees could not exceed 25 percent of the benefit provided to all employees.<br><br>Effective date.--Taxable years beginning after December 31, 1984. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 1. Welfare Benefit Plans<br><br>d. Coordination with treatment of deferred compensation | Deductions for contributions to a nonqualified deferred compensation plan are not allowed until a benefit is includible in the employee's income, but the Code does not provide a clear distinction between deferred compensation and welfare benefits. | | Deferred compensation would include any arrangement for deferring the receipt of compensation or any unfunded deferred benefit.<br><br>Effective date.--Amounts paid or incurred after March 31, 1984. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| 2. Treatment of management unions | The nondiscrimination rules for qualified pension plans and statutory fringe benefits generally provide that nondiscrimination rules do not apply to employees covered by a collective bargaining agreement. Recently, organizations of management employees have claimed such status and have established plans that discriminate in favor of highly-paid employees. | | Present law could be clarified to prevent organizations consisting primarily of owners, officers, or executives of the employer from using exclusions designed for legitimate collective bargaining units.<br><br>Effective date.--April 1, 1984. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 3. Pension plans consisting only of employee contributions | Nondeductible contributions may be made by an employee under a qualified pension plan or tax-sheltered annuity (within limits) and may generally be withdrawn without penalty by the employee at any time permitted by the plan. The investment earnings on nondeductible employee contributions are not taxed until distributed. If a distribution occurs before pension benefits start, the employee contributions, withdrawals of which are tax free, are considered to be distributed before any taxable income. Recently, some employers have adopted qualified retirement plans under which all contributions are made by employees. These plans permit withdrawals to be made by check or credit cards at any time. The plans often are regarded as checking accounts with tax-free investment income. | | A pension plan substantially all of the accrued benefits of which are attributable to employee contributions would not be considered to be a qualified plan.<br><br>Effective date.--Plan years beginning after March 31, 1984. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 4. Nondiscrimination rules for cash-or-deferred arrangements | Under a cash-or-deferred arrangement (a Sec. 401(k) plan), discrimination is measured by comparing tax-free elective deferrals by the highest paid 1/3 of employees with the deferrals by the other employees. In some cases, employees with low or moderate pay fall into the upper 1/3 group, which may permit larger deferrals by other members of the top 1/3 group. In addition, despite legislative history indicating a contrary intent, employer social security contributions may be taken into account under a sec. 401(k) plan in testing for discrimination. | | Social Security contributions could be excluded in determining whether a cash-or-deferred arrangement is nondiscriminatory.<br><br>Effective date.--Plan years beginning after December 31, 1984. |
| 5. Revenue effect of employee benefit items | | | Revenue effect.<br><br>Fiscal Years, 1984-1987<br>[Billions of Dollars]<br>1984 1985 1986 1987 84-87<br>* 0.1 0.2 0.3 0.6 |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 1. Avoidance of rules relating to transfers of depreciable property between related taxpayers | In order to prevent tax-motivated transactions, transfers between related parties often receive special treatment under the Internal Revenue Code. One provision provides that a transferor will be treated as receiving ordinary income rather than capital gain on the transfer of property to a related party when that property is depreciable property in the hands of the transferee (section 1239).<br><br>The courts have held that the transfer of a patent application as opposed to a patent does not fall within this anti-abuse rule because the application itself is not depreciable property (Lan Jen Chu v. Commissioner, 486 F.2d 696 (1st Cir., 1973)). However, once the application is granted, the transferee can depreciate the resulting patent. | | The provision of the Code relating to gains from the sale of depreciable property between related parties (section 1239) could be amended to treat a patent application as depreciable property, thus requiring that any gain recognized to the transferee be treated as ordinary income rather than capital gain.<br><br>That provision could also be broadened to cover sales between a taxpayer and a trust in which the taxpayer or the taxpayer's spouse have a beneficial interest (other than a remote contingent interest).<br><br>Effective date.--Transfers after date of Committee action.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br><br>* .1 .2 .3 .6 |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 2. Collapsible corporations | In general, a collapsible corporation is one formed or availed of principally for the manufacture, construction, production, or purchase of certain types of property with the view to the sale or exchange by the shareholders of their stock (or of the liquidation of the corporation) before the realization by the corporation of a "substantial" part of the taxable income to be derived from such property. If a stock in a collapsible corporation is sold, exchanged, or the corporation is liquidated in whole or in part (i.e., collapsed), or in the case of certain distributions, any gain recognized by any shareholder in any such sale, exchange, liquidation, or distribution which would otherwise be long-term capital gain is considered ordinary income.<br><br>Under court decisions, a corporation will have realized a "substantial" part of the taxable income to be derived from the property if the corporation realizes as little as one-third of the taxable income to be derived from the property. Present law also provides an exception to collapsible corporation treatment (the "70/30" rule). In general, under this rule, if 70 percent or less of a shareholder's total gain in a | The substantial part requirement would be defined to be "two-thirds" of the taxable income to be derived from the property.<br><br>Conforming changes will be made to the "70/30" rule to prevent corporations from otherwise avoiding the collapsible corporation provision.<br><br>Effective date.--Date of enactment.<br><br>Revenue effect.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>-- * 0.1 0.2 0.3 | |

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| | taxable year is attributable to collapsible assets of the corporation, then none of the recognized gain in such year is treated as ordinary income.<br><br>(H.R. 4170 contains similar rules with respect to gain from condominium conversions.) | | |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 3. Payment of Excise Tax Revenues to Puerto Rico and the Virgin Islands. | A special excise tax is imposed on articles coming into the U.S. from Puerto Rico and the Virgin Islands. The tax is equal to the excise tax imposed on like articles of U.S. manufacture.<br><br>Revenues from the special tax are paid to Puerto Rico and the Virgin Islands.<br><br>Puerto Rico presently conducts a program under which distilled spirits from the U.S. are redistilled in Puerto Rico and reshipped to the U.S., thereby enabling Puerto Rico to receive an excise tax payment. | No proposal. | Revenues from excise tax on articles coming into the U.S. from Puerto Rico and the Virgin Islands would be paid to those possessions only in the following cases--<br><br>(1) In the case of distilled spirits, if at least 90 percent of the distilled spirits were originally distilled in Puerto Rico or the Virgin Islands;<br><br>(2) In the case of any article subject to Federal excise tax which comes into the U.S. from Puerto Rico, if 50 percent or more of the value of the article is attributable to Puerto Rican input;<br><br>(3) In the case of any article subject to Federal excise tax, if the applicable possession provides no subsidy to the industry involved of a kind different from that provided to industry generally.<br><br>A general exemption would be provided for rum; cane neutral spirits would be exempt from tests 2 and 3. |

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| | | | Effective date.--the proposal generally would apply to articles coming into the U.S. after March 1, 1984.<br><br>A transition rule would permit rebates with respect to $50 million tax on redistilled spirits coming into the U.S. from Puerto Rico between March 1, 1984, and July 1, 1984.<br><br>Reduced spending.--<br><br>Fiscal Years, 1984-87<br>[Billions of Dollars]<br><br>1984 1985 1986 1987 84-87<br>.1 .2 .2 .3 .8 |

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| | The tax straddle rules require the deferral of losses from certain actively traded personal property or positions in such property, to the extent the taxpayer has unrecognized gain at the close of the taxable year on offsetting positions. Positions are offsetting if there is a substantial diminution in the risk of loss from holding one position because the taxpayer holds the other position. | | |
| 1. Straddles in stock options. | Stock and stock options traded on U.S. exchanges that have an exercise period less than the minimum long-term capital gain holding period are excluded from the loss deferral and other straddle rules. Because the long-term holding period is one year and exchange traded options have a maximum exercise period of approximately nine months, all such options are excluded from the straddle rules. | For investors (other than professional options traders or market makers) apply the loss-deferral rule to straddles consisting of offsetting positions in exchange-traded stock options or stock and an offsetting stock option position, with an exception for covered call options that are not deep-in-the-money.<br><br>In addition, the holding period of stock would not run if the taxpayer grants an in-the-money option to buy stock held by the taxpayer.<br><br>Effective date.--Positions established after October 31, 1983. | Extend the loss deferral rule to any straddle involving stock, except a straddle all of the legs of which are stocks.<br><br>In lieu of [illegible] the holding period of optioned stock, recharacterize any long-term gain on the stock to the extent of any short-term loss on the option. |

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| 2. Market makers. | | | |
| (a) Characterization of gains and losses | Options traders on security exchanges.--Gain or loss from transactions in options written or acquired by options market makers (or professional options traders) are treated as ordinary income or loss.<br><br>Commodity traders.--Historically, professional commodity traders have been treated as realizing capital gain or loss from their transactions. For commodity traders, each regulated futures contract held at the end of the taxable year is treated as if it were disposed of at its fair market value, and any gain or loss is taxed as if it were 60 percent long-term and 40 percent short-term, resulting in a maximum tax rate of 32%. | Tax options market makers (or professional options traders) under a mark-to-market system. Tax rates currently applicable to options professionals (a maximum rate of 50 percent) would be retained.<br><br>Effective date.--Positions established after the date of enactment. | Extend the 32-percent maximum tax rate available to professional commodity traders to professional options traders.<br><br>Provide expressly that both professional options traders and professional commodity traders are to be treated as buying and selling capital assets. |

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| (b) Hedging exemption | Options market makers are exempted from the tax straddle rules with respect to transactions entered into for the purpose of maintaining hedged positions. Moreover, an options trader is considered to be a dealer in property subject to the option. | No proposal. | Provide that the hedging exemption would not apply to options traders unless they are dealers with respect to the underlying property. For all persons who claim the hedging exemption, limit the deductibility of ordinary losses from hedging transactions to income derived in the conduct of the trade or business to which the hedging relates. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 3. Mixed straddles | In the case of a straddle consisting of an RFC (gain on which is taxable at a maximum rate of 32 percent) and a non-RFC (gain on which is taxable at a maximum rate of 50 percent), depending on which leg of the straddle generates gain, unrelated short-term capital gain can be converted to long-term capital gain and unrelated long-term capital gain can be converted to short-term capital gain.<br><br>Treasury is provided with regulatory authority to prevent the conversion of short-term capital gain to long-term capital gain. | No proposal. Regulations have not yet been issued. | Broaden Treasury's regulatory authority to permit correction of inequities. |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| 4. New options products | | | |
| (a) cash-settlement options | It is unclear whether the tax rules for the taxation of options apply to exchange-traded options that settle only in cash. Taxpayers with losses on these options may claim ordinary loss treatment. | Clarify present law to provide expressly for capital gain or loss treatment on transactions in cash-settlement options.<br><br>Effective date.--Positions established after October 31, 1983. | |
| (b) Options on futures | Regulated futures contracts (RFCs) traded on domestic boards of trade designated as contract markets by the Commodity Futures Trading Commission are marked to market at the close of the taxable year and treated as 60 percent long-term capital gain or loss and 40 percent short-term capital gain or loss, resulting in a maximum tax rate of 32 percent. Some taxpayers claim that options on RFCs constitute RFCs, while other taxpayers claim that options on RFCs are subject to the general rules for the taxation of options (taxable at a maximum rate of 50 percent). | Provide that gain or loss is recognized upon the exercise of an option on an RFC.<br><br>Effective date.--Positions established after the date of enactment. | Tax options on RFCs under the mark-to-market system applicable to RFCs (at a maximum tax rate of 32 percent). |

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| c. Exchange-traded options | Exchange-traded options are subject to the general rules for the taxation of options (taxable at a maximum rate of 50 percent), and the tax straddle rule that requires loss deferral. | Retain present law for all exchange-traded options. | |
| (i) Equity based options | | Retain present law. | Options on narrow-based stock indexes and options on individual stocks held by investors would remain subject to the general rules (including the loss deferral rule).<br><br>Options on broad-based stock indexes would be subject to mark-to-market with a 32-percent maximum rate. |
| (ii) Nonequity based options | | Retain present law. | Tax all nonequity based listed options under the mark-to-market system. Extend the 32 percent maximum tax rate applicable to professional commodity traders to holders of nonequity based listed options. |

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| 5. Elections | When the mark-to-market system was enacted, commodity traders were given elections to apply the mark-to-market rules to positions held on or before the date of enactment. Under one provision, taxpayers could elect to apply the rules to all positions held during the taxable year that included the general effective date. If this election was made, any net tax liability could be paid in five equal annual installments, with interest. Under the other provision, taxpayers could elect to apply the rules to all positions held on the general effective date. | No proposal. | Provide transitional rules. |

## IV. HIGHWAY USE AND DIESEL FUEL TAXES

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
|---|---|---|---|
| Heavy vehicle use tax | Under 33,000 lbs.--no tax; | | |
| 1. Tax rate effective July 1, 1984. | 33,000-55,000 lbs.--$50 per year, plus $25 per 1,000 lbs. over 33,000 lbs.; | Under 55,000 lbs.--no tax; | Under 55,000 lbs.--no tax; |
| | 55,000-80,000 lbs.--$600 per year, plus $40 ($44 on July 1, 1986, $48 on July 1, 1987, $52 on July 1, 1988) per 1,000 lbs. over 55,000 lbs.; | 55,000-80,000 lbs.--$50 per year, plus $24 per 1,000 lbs. over 55,000 lbs. | 55,000-72,000 lbs.--$150 per year, plus $20 per 1,000 lbs. over 55,000 lbs. |
| | Over 80,000 lbs.--$1,600 per year ($1700 on July 1, 1986, $1,800 on July 1, 1987, $1,900 on July 1, 1988). | Over 80,000 lbs.--$650 per year | Over 72,000 lbs.--$500 per year |
| 2. Special rules for small owners. | Tax rate for year beginning July 1, 1984, is $3 per 1,000 lbs. if 26,000 lbs. or more; | Same as present law. | Tax rate for year beginning July 1, 1984, is $3 per 1,000 pounds if 55,000 lbs. or more |
| | Tax rate after June 30, 1985, same as general tax rate with 1-year delay; | Tax rate after June 30, 1985, same as general rate (item 1) | Tax rate after June 30, 1985, same as general rate (item 1) |
| | 5,000-mile exemption and proration for theft or casualty not effective until July 1, 1985. | Same as present law. | 5,000-mile exemption and proration for theft or casualty effective July 1, 1984 |

| Item | Present Law | Administration Proposal | Possible Modifications and Other Proposals |
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| Highway diesel fuel tax | | | |
| 3. Rate of tax through September 30, 1988. | 9 cents per gallon | 15 cents per gallon, effective July 1, 1984 (i.e., diesel differential of 6 cents per gallon) | 14.5 cents per gallon, effective July 1, 1984 (i.e., diesel differential of 5.5 cents per gallon) |
| 4. Exemption from diesel differential for fuel used in vehicles under 10,000 lbs. | | Rebate of actual diesel differential paid or standardized amount for year, claimed annually on income tax form of payee. | Rebate of standardized amount for life of vehicle, claimed one time on income tax form of owner. |